TESTIMONY OF
PETER R. MERRILL

Before the

House Budget Committee

July 22, 2004

COMPETITIVENESS OF THE U.S. TAX CODE

I. INTRODUCTION

I am Peter Merrill, Principal and Director of the National Economic Consulting group at PricewaterhouseCoopers LLP. I am testifying today on my own behalf and not as a representative of any organization.

The focus of my testimony is on the competitiveness of the U.S. tax system, which I assess through a comparison of the structure of the U.S. tax system with that of the 30 member countries of the Organization for Economic Cooperation and Development (OECD). In a global economy, differences in tax systems can affect international capital flows—to the benefit or detriment of a country's workers and investors.

In some instances, U.S. rules regarding the taxation of both domestic and foreign income are out of step with the tax systems used by other major industrial countries.

II. TAX COMPETITIVENESS IN A GLOBAL ECONOMY

Much of the U.S. tax system was developed when the United States dominated the global economy. This is no longer the case. In the 1960's, the U.S. economy represented 40 percent of global GDP and U.S. multinationals accounted for 50 percent of cross-border investment. In 2003, the U.S. economy represented 30 percent of global GDP and U.S. multinationals accounted for less than 22 percent of cross border investment (see Exhibit 1).

The U.S. economy is also far more open to trade and investment than was the case just a few decades ago. Merchandise trade (imports plus exports) has increased from less than 7 percent of GDP in the 1960s to 18.6 percent over the last four years. From 1980 to 2002, the stock of U.S. direct investment abroad increased (in nominal dollars) from $390 billion to $1.84 trillion (370 percent), while foreign direct investment in the United States increased from $130 billion to $1.50 trillion (1080 percent). The growth in the stock of cross-border portfolio investment is even more staggering. From 1980 to 2002, private investment in foreign securities increased from $62 billion to $1.8 trillion (2855 percent), while foreign private investment in U.S. securities increased from $90 billon to $3.2 trillion (3500 percent) (see Exhibit 1).

As a result of the growing importance of international capital flows, U.S. tax policy is no longer insulated from global market forces. Increasingly, one of the considerations in the design of a country's tax system must be how it compares with that of its major trading partners. And, there is little doubt that governments react to changes in the tax systems of their trading partners. For example, the reduction in the U.S. corporate income tax rate from 46 percent to 34 percent under the 1986 Tax Reform Act precipitated similar reductions in many other OECD countries. Another example is the spread of the value-added tax systems from the European Union to over 120 countries worldwide.

Competitiveness is one of a number of criteria by which to judge the U.S. tax system—other traditional criteria include fairness, simplicity, efficiency, and revenue adequacy. The focus of this testimony is on how the U.S. tax system compares with that of other major industrial countries.

III. INTERNATIONAL COMPARISON OF TAX STRUCTURES

A. Aggregate Revenues and Expenditures

The United States is a relatively low tax country. According to OECD statistics, as of 2001, the total tax burden in the United States—federal, state, and local combined—was 28.9 percent of GDP, fourth lowest among the 30 OECD countries (see Exhibit 2). The favorable tax burden reflects the smaller role that government plays in the U.S. economy, where government expenditures relative to GDP were fourth lowest among the OECD countries. The publicly-financed share of expenditures on health and post-secondary education generally is higher outside the United States and correspondingly greater government revenues are required to finance these outlays.

In January of this year, the Congressional Budget Office estimated that federal government revenues would fall short of federal government expenditures by 3.0 percent of GDP in fiscal year 2005, but that the federal government deficit would be eliminated by 2014. This forecast, however, assumes that all of the temporary provisions in EGTRRA and JGTRRA expire as scheduled and excludes the Medicare prescription drug benefit enacted earlier this year.

B. Aggregate Debt

According to 2001 OECD statistics, outstanding marketable debt of the United State government was less than the average OECD country by 12.7 percent of GDP.[1] In January of 2004, CBO projected that by 2009, federal debt held by the public would increase by 7.6 percentage points of GDP relative to the 2001 level. This forecast assumes that all expiring provisions expire as scheduled and excludes the new Medicare prescription drug benefit.

C. Composition of Revenues

While the United States is a relatively low tax country, it relies more heavily on taxes on income and profits—both as a share of total taxation and as a share of GDP—than the average OECD country. Combining all levels of government, income and profits taxes accounted for about 48 percent of U.S. revenues in 2001 as compared to 36 percent for the average OECD country (see Exhibit 3). Income and profits taxes collected at all levels of government amounted to 14.1 percent of GDP in the United States in 2001 as compared to 13.4 percent for the average OECD country (see Exhibit 4)

The federal government is even more heavily reliant on income and profits taxes as there is no broad base consumption tax, like the retail sales tax used in 45 states and the District of Columbia. Indeed, the United States is the only OECD member country that does not have a national value-added or goods and services tax.

From a trade perspective, heavy reliance on income taxes relative to consumption taxes may be viewed as disadvantageous because World Trade Organization (WTO) rules only permit border tax adjustments (i.e., exemption of exports and taxation of imports) on indirect taxes. Absent

[1] OECD, *OECD in Figures: Statistics on the Member Countries*, 2003.

border adjustments, taxes may distort the composition if not the volume of trade.[2] An important reason to avoid over-reliance on income and profits taxes is that they discourage savings and investment, and thus suppress long-run economic growth.

D. Personal Income Tax

The average OECD central government imposed a top personal income tax rate of 37.6 percent in 2003 (see Exhibit 5). In the United States, the top federal tax rate on ordinary income is 35 percent, less than the OECD average. However, unlike most of the OECD countries, individuals in the United States typically are subject to income tax by both federal and state levels of government.

Unless the sunset in the 2001 Act is removed, the top federal individual income tax rate will increase to 39.6 percent in 2011. This would put the United States 2 percentage points above the current average for OECD countries.

High marginal income tax rates discourage savings and work effort—particularly of secondary workers—and encourage tax avoidance and evasion. Moreover, countries with high personal income taxes are unattractive places to locate facilities with high-paying jobs such as corporate headquarters and research facilities.

E. Corporate Income tax

Immediately following the Tax Reform Act of 1986, which lowered the U.S. corporate income tax rate from 46 to 34 percent, the U.S. rate was relatively attractive. This is no longer true today. The U.S. corporate income tax rate increased to 35 percent in 1991, while the average OECD country's corporate rate fell to 29.3 percent in 2003—5.7 percentage points less than the U.S. rate. The average corporate rate for the 25 members of the newly expanded European Union is just 26.3, 8.4 percentage points less than the U.S. rate (see Exhibit 6). The United States is tied with Spain and Greece for third highest corporate income tax rate among the 30 OECD countries. Unlike most OECD countries, the United States imposes corporate income taxes at the state and, in some cases, local levels of government. Taking into account multi-level corporate income taxes, the disparity between the U.S. rate and the OECD average is likely greater.

Despite relatively high rates, the U.S. corporate income tax raises relatively little revenue. In 2001, U.S. corporate income tax receipts amounted to just 1.9 percent of GDP compared to the OECD average of 3.5 percent of GDP). U.S. corporate income tax receipts were suppressed in

[2] A theoretical framework is set forth in, Martin Feldstein and Paul Krugman, "International Trade Effects of Value Added Taxation" (with Paul Krugman) in *Taxation in the Global Economy*, Assaf Razin and Joel B. Slemrod, (eds.), the University of Chicago Press, 1990. Consistent with the standard theoretical model, empirical research finds there is *no* export or trade advantage for countries with greater reliance on value-added taxes. In fact, Hines and Desai find a negative relationship which the authors attribute to two implementation features of VAT systems: VATs tend to be imposed at higher rates on traded than non-traded goods and exporters often receive incomplete VAT rebates *See*, James R. Hines, Jr. and Mihir A. Desai, "Value Added Taxes and International Trade: The Evidence," (November 2002) presented at December 2002 Brookings/ITPF conference on Tax Systems and International Trade (www.itpf.org/presearch_itpindex.htm).

2001 by the recession, the fall in the stock market, the terrorist attack of September 11, and the temporary adoption of bonus depreciation and extended loss carrybacks.

High corporate income tax rates are economically unattractive for a number of reasons. First, high corporate income tax rates make the United States a relatively unattractive location for corporate investment. In a global economy, countries with high corporate income tax rates may suffer a declining share of worldwide investment and reduced employment opportunities for local workers. Second, high corporate income tax rates encourage the shifting of income abroad. Within the limits of existing rules, companies have an incentive to establish inter-company prices and corporate financial structures that locate income away from high-tax jurisdictions. Third, the incentive to engage in tax planning increases the higher the tax rate, which reduces the corporate revenue yield and diverts valuable resources away from more economically productive activities.

Double Taxation of Corporate Income

In a tax system where corporate income is taxed a second time when paid as dividends to shareholders, high corporate income tax rates discourage businesses from operating in regular corporate form. While the 2003 Act reduced the shareholder level tax on corporate dividends, this relief is scheduled to sunset after 2008. If dividend relief is allowed to sunset, the United States would join Switzerland as the only OECD countries without double taxation relief and the top rate of income tax on dividends—combining federal and individual level taxation—would increase from 44.75 percent today to over 60 percent after 2010 (see Exhibits 7 and 8).

F. Payroll Taxes

Payroll taxes provide the primary source of funding for the Social Security, Medicare, and federal and state unemployment insurance systems. Social insurance and payroll taxes represent about one-fourth of government revenues in the United States, similar to the average for all OECD countries. While the expenditures from social insurance programs are progressive, the payroll tax is regressive. However, the regressivity of the federal payroll tax is mitigated by the earned income tax credit, which is a refundable income tax credit targeted at low-income workers. In addition, the portion of the federal payroll tax dedicated to hospital insurance (imposed at 1.45 percent rate on employees and employers) is not subject to the wage cap that applies to the balance of social security taxes (imposed at a 6.2 percent on employers and employees).

Future Revenues and Outlays of the Social Insurance System

Like many other advanced industrial economies, the projected increase in the obligations of the U.S. social insurance system are far greater than the revenue stream that will be generated by existing funding sources. In 2003, the General Accounting Office estimated that future liabilities for the Social Security and Medicare systems would exceed future revenues for these program by $20.7 trillion in present value, not including the new Medicare prescription drug benefit enacted earlier this year (see Exhibit 9).[3] This unfunded liability amounts to over $71,000 for every U.S. citizen.

[3] U.S. General Accounting Office, *Financial Statement of the United States Government*, 2003.

G. Consumption and Excise Taxes

The United States is one of the few countries that does not have a national level value-added or goods and services tax. The main form of consumption tax is the retail sales tax which is imposed by 45 states and the District of Columbia as well as approximately 7400 local jurisdictions. The retail sales tax system has a number of disadvantages as compared to the VAT. In particular, the retail sales tax excludes most services and, unlike the VAT, cannot be fully recovered by business purchasers, with the result that the tax can cascade through the production/distribution chain.

IV. TAXATION OF INCOME FROM U.S. DIRECT INVESTMENT ABROAD

A. Do the Foreign Operations of U.S. MNCs Hurt the Domestic Economy?

If taxes make the United States an unattractive location to headquarter a multinational corporation, then U.S. multinationals will lose global market share. This loss in global market share can happen in a variety of ways. First, U.S. individual and institutional investors can choose to invest in foreign rather than U.S. headquartered companies. Second, in a cross-border merger, the transaction may be structured as a foreign acquisition of a U.S. company rather than the reverse. By choosing to be headquartered abroad, the merged entity can invest outside the United States without being subject to the complex and onerous U.S. rules that apply to the foreign source income of U.S.-headquartered companies.[4] Third, and most starkly, a number of U.S. companies have structured transactions in which their U.S. parents are acquired by their own foreign subsidiaries. Such "inversion" transactions, like foreign acquisitions of U.S. companies, allow new foreign investments to be structured as subsidiaries of a foreign parent corporation and thus not subject to U.S. rules relating to the taxation of foreign source income. Fourth, new ventures can be incorporated at inception as foreign corporations.

A decline in the market share of U.S. multinationals would adversely affect domestic workers. U.S. multinationals play an important role in promoting U.S. exports and creating high-wage jobs. According to the U.S. Commerce Department, in 2001, U.S. multinationals were directly responsible, through their domestic and foreign affiliates, for $425 billion of U.S. merchandise exports—almost 60 percent of all merchandise exports. The role of multinationals in promoting exports is corroborated by an OECD study which found that each dollar of outward foreign direct investment is associated with $2.00 of additional exports.[5] Dartmouth professor Mathew Slaughter has found that over the 10-year period 1991-2001, jobs added by U.S. multinationals abroad were matched almost two for one by U.S. jobs added in their parent operations.[6] Moreover, Slaughter finds that U.S. multinationals increased their domestic employment at a faster pace than U.S. companies without foreign affiliates—evidence that the foreign operations of U.S. multinationals *increase* domestic job growth. As noted by David Riker and Lael Brainard:

---

[4] Note that, absent restructuring, the existing foreign operations of a U.S. company acquired by a foreign company remain subject to U.S. tax rules.

[5] OECD, *Open Markets Matter: The Benefits of Trade and Investment Liberalization*, p. 50 (1998).

[6] Mathew J. Slaughter, "Globalization and Employment by U.S. Multinationals: A Framework and Facts," *Daily Tax Report*, March 26, 2004, section J, pp. 1-7.

> "Specialization in complementary stages of production implies that affiliate employees in industrialized countries need not fear the multinationals' search for ever-cheaper assembly sites; rather, they benefit from an increase in employment in developing country affiliates."[7]

U.S.-based multinationals account for 20 percent of domestic employment, and locate 77% of their global production and 80% of the global capital spending at home.[8] In addition, multinational companies pay their domestic workers more than comparable U.S. companies without international operations.[9]

B. Comparison of U.S. and Foreign Country Rules for Taxing Multinational Income

Compared to major competitor countries, the United States is a relatively unattractive jurisdiction in which to locate the headquarters of a multinational company. Quantitative evidence of this comes from a study published by the European Commission in 2001 which found that, on average, U.S. multinationals bear a higher effective tax rate—ranging from three to five percentage points--when investing into the European Union than do multinationals headquartered in the EU (see Exhibit 10).

Aside from the relatively high U.S. corporate income tax rate, there are a number of features of the U.S. system of taxing foreign source income that depart from international norms.

Worldwide tax system. Over half of the OECD countries have dividend exemption ("territorial") tax systems under which a parent company generally is not subject to tax on the active income earned by a foreign subsidiary (see Exhibit 11). By contrast, the United States generally taxes income earned through a foreign corporation when repatriated.[10] Moreover, the United States is the only OECD country that does not exempt the foreign earned income of its citizens who reside abroad, making it more expensive for U.S. multinationals to send employees on international assignments.[11]

Foreign tax credit limitations. The U.S. foreign tax credit, which is intended to prevent double taxation of foreign source income, has a number of deficiencies that increase complexity and prevent full double tax relief, including:[12]

---

[7] David Riker and Lael Brainard, *U.S. Multinationals and Competition from Low Wage Countries*, National Bureau of Economic Research Working Paper no. 5959 (1997) p. 19.

[8] Laura D'Andrea Tyson, "Why The Trade Deficit May Not Loom So Large," *BusinessWeek*, June 7, 2004

[9] Doms and Jensen find that U.S. plants of companies without foreign operations pay production workers 10-15 percent less and nonproduction workers 5-7 percent less than comparable plants of U.S. multinational companies, controlling for industry, size of company, and state where the plant is located. *See*, Mark Doms and Bradford Jensen, *Comparing Wages, Skills, and Productivity between Domestic and Foreign-Owned Manufacturing Establishments in the United States*, mimeo. (October 1996).

[10] I am unaware of any OECD country that requires formula apportionment of domestic interest expense to exempt foreign dividends with the result that this portion of domestic interest expense is nondeductible. Grubert and Mutti find that adoption of a dividend exemption system with formula apportionment of domestic interest expense would actually increase the U.S. tax burden attributable to foreign source income. *See*, H. Grubert and J. Mutti, *Taxing International Business Income: Dividend Exemption versus the Current System*, American Enterprise Institute, 2001.

[11] *See*, Price Waterhouse, "Economic Analysis of the Foreign Earned Income Exclusion," 1995.

[12] See, National Foreign Trade Council, *U.S. International Tax Policy for the 21st Century*, vol. 1, Part II, 2001

- Over allocation of U.S. interest expense against foreign source income due to failure to take into account foreign debt. This reduces the foreign tax credit limitation and can cause income that has been subject to foreign tax at a rate of 35 percent or more to be subject to additional U.S. tax;
- Asymmetric loss recapture rules that have the effect of restoring U.S. but not foreign income, thereby reducing the foreign tax credit limitation;
- The limitation on foreign tax credits to 90 percent of alternative minimum tax liability;
- The limited carryover period for foreign tax credits (two years back and five years forward); and
- The complexity associated with the numerous separate foreign tax credit limitations and the "high-tax kick out" rules that move certain income out of the passive basket.

U.S. anti-deferral rules. Another difference from the multinational tax rules of other countries is the unusually broad scope the U.S. anti-deferral rules under subpart F. While most countries tax passive income earned by controlled foreign subsidiaries, the United States is unusual in taxing a wide range of unrepatriated *active* income as a deemed dividend to the U.S. parent, including:[13]

- Foreign base company sales income;
- Foreign base company services income;
- Foreign base company shipping income; and
- Active financial services income (a temporary exclusion of this income from Subpart F will expire for taxable years beginning after 2006).

Moreover, the U.S. anti-deferral system is extraordinarily complex, with multiple and overlapping rules including separate regimes for: controlled foreign corporations (CFCs), passive foreign investment companies (PFICs), foreign personal holding companies (FPHCs), foreign investment companies (FICs), and Personal Holding Companies (PHCs).[14]

The net effect of these differences between U.S. tax rules and international norms, is that U.S. multinationals frequently pay a greater share of income in foreign and U.S. tax than do competing multinationals headquartered outside of the United States.

C. Recent Legislative Proposals

The ETI replacement bills adopted earlier this year by the House and Senate contain international tax reform provisions that would address many of the aspects of U.S. tax law that depart from international norms in ways that adversely affect the competitiveness of U.S. multinationals.

Foreign tax credit.—Both bills alleviate the double taxation of foreign source income through measures addressing interest allocation, recharacterization of domestic losses, and removing the

[13] *Ibid*., vol. 1, Part I.

[14] See, Carl A. Dubert and Peter R. Merrill, *Taxation of U.S. Corporations Doing Business Abroad: U.S. Rules and Competitiveness Issues (Second Edition)*, FEI Research Foundation, 2001.

90-percent limitation in the AMT. The House bill also reduces the number of separate foreign tax credit limitation categories, while the Senate bill extends the carryforward period for foreign tax credits to 20 years, consistent with net operating losses.

Anti-deferral rules.—Both bills reduce the taxation of active foreign income that is reinvested abroad by "looking through" payments between related CFCs to determine their character and by excluding certain active foreign shipping and aircraft income from Subpart F. Both bills also simplify compliance with Subpart F by repealing the FPHC and FIC rules and the PHC rules applicable to foreign corporations. In addition, the Senate bill simplifies compliance by increasing the de minimis exemption from Subpart F.

V. COMPLEXITY

The burden of the tax system includes not only the amount that taxpayers are obliged to remit to the government but also the time and money cost of compliance, including researching and monitoring changes in tax laws and regulations, collecting information required for return preparation, preparing and filing the return, record retention, and responding to audits. Compliance costs were estimated by the Tax Foundation to increase the burden of the federal income tax by 20.4 percent, or $194 billion in 2002.[15] By comparison, estimates of the compliance costs imposed by the retail sale taxes typically are on the order of 3-4 percent of revenues.[16]

Some of the complexity of the income tax system is inherent in measuring taxable income in a technologically advanced and globally integrated economy. There are few remedies for this inherent complexity short of adopting an alternative basis of taxation, such as consumption.

Proliferation of Special Purpose Deductions, Credits, and Exemptions

One important source of complexity is a policy choice—the use of special purpose deductions, credits, and exemptions in the Code to encourage certain types of economic activities or to redistribute income to specific groups of taxpayers judged needy of assistance. Many of the policy objectives underlying these special purpose deductions, credits and exemptions could be achieved through federal spending programs, subject to the Congressional authorization and appropriations process, and administered by federal agencies other than the IRS.

Alternative Minimum Tax

Re-designed in 1986, the alternative minimum tax (AMT) for individuals and corporations operates like a parallel tax system. Taxpayers compute tax liability twice: under the regular system and under the AMT system, with its own separate tax base and rates. AMT liability is equal to the excess, if any, of tax liability under the AMT system over the regular system.

---

[15] Scott Moody, "The Cost of Tax Compliance," *Tax Foundation*, February 2002. Using a different methodology, Prof. Joel Slemrod estimated the private sector collection cost of the U.S. income tax system at $125 billion in 2004. *See*, Joel Slemrod, "Written Testimony submitted to the Committee on Ways and Means, Subcommittee on Oversight, Hearing on Tax Simplification," June 15, 2004.

[16] Tax Administrator News, 1993.

Certain AMT payments may be carried forward and used to offset regular tax in future years to the extent in excess of liability determined under the alternative system.

On its face, the AMT system is inherently complex as it requires calculation of tax liability under two different systems. It imposes compliance burdens on all taxpayers—whether or not AMT is owed—because, in principle, they must calculate hypothetical liability under the alternative system to determine whether AMT is due and whether the use of tax credits under the regular tax system is constrained by the AMT.

Worse still, for individuals, the AMT is becoming far more pervasive because (1) the dollar amount of the AMT exemption was not indexed in 1986, and (2) the regular tax rates but not the AMT rates were reduced in 2001 and 2003. As a result, CBO estimates that the number of returns affected by the AMT will increase from 3 million in 2004 to 29 million in 2010.[17]

Fixing the AMT is a serious budgetary challenge. The Congressional Budget Office has estimated that indexing the AMT exemption amount at 2004 levels would cost $376 billion over the next 10 years.[18]

Tax Code Instability

Another source of compliance burden is the frequency of changes in the tax Code. According to the Tax Foundation, from 1995 to 2000, the tax Code increased by 182 pages, about half the pages of the entire 1954 Code. At this rate, the Code will increase from 1670 pages in 2000 to about 2600 pages in 2010.

Tax Code instability also is due to the adoption of tax provisions on a temporary basis to comply with budgetary scoring rules. These sunsets create uncertainty and impose real costs on taxpayers. The most absurd example is the scheduled repeal of the estate and gift tax in 2010 and re-enactment in 2011. This is an example of how rules designed to promote fiscal responsibility have had the side effect of creating tax structure instability.

Foreign Source Income

As noted in the Administration's FY 2003 Budget, one of most complex aspects of corporate taxation is the treatment of foreign source income. A survey of Fortune 500 companies found that 43.7 percent of U.S. income tax compliance costs were attributable to foreign source income even though foreign operations represented only 26-30 percent of worldwide employment, assets and sales.[19] These high compliance costs are a hidden form of taxation that discourages small U.S. companies from operating abroad and makes it more difficult for larger companies to compete successfully with foreign multinationals.

VI. SUMMARY

[17] CBO, *The Budget and Economic Outlook, Fiscal Years 2005 to 2014*, January 2004, p. 81.
[18] *Ibid*. pp. 5-7.
[19] Marsha Blumenthal and Joel Slemrod, "The Compliance Costs of Taxing Foreign-Source Income: Its Magnitude, Determinants, and Policy Implications, *International Tax and Public Finance*, vol. 2, no. 1, 37-54 (1995).

This testimony supports the following conclusions:

- U.S. residents currently pay a smaller share of GDP in total taxes than do residents of most other OECD countries.
- However, the present U.S. tax structure does not generate sufficient revenue to meet projected federal spending in the long run.
- Closing the fiscal gap by raising income and profit taxes would cause the U.S. tax system to depart even further from international norms, as the United States already relies much more heavily on income and profit taxes—both as a percent of GDP and as a percent of total taxes—than the average OECD country.
- The U.S. corporate income tax rate is tied with Greece and Spain as third highest among the OECD countries.
- If the 2001 and 2003 Act sunsets are not reversed, the top central government individual income tax rate in the United States will by 2011 jump to 2 percentage points above the current average for OECD countries.
- According to the Tax Foundation, the cost of complying with the federal income tax system increases the U.S. tax burden by 20 percent. This is much higher than estimates of the cost of complying with VAT and retail sales tax systems.
- A particularly worrying source of tax complexity is the estimated increase in the number of individual returns affected by the AMT from 3 million in 2004 to 29 million in 2010.
- The U.S. international tax rules are out of step with competitor countries. The U.S. system of taxing worldwide income is extremely complex and imposes high compliance costs relative to revenue raised.

Exhibit 1.—The United States in the World Economy

U.S. International Trade (percent of GDP)[1]	**1960-69**	**1990-99**	**2000-2003**
Merchandise exports	3.7	7.3	7.0
Merchandise imports	3.1	9.6	11.6
Trade openness: merchandise exports plus imports	6.8	16.9	18.6

U.S. International Investment Position ($ billions)[2]	**1980**	**1997**	**2002**
Net international investment position	360.8	-820.7	-2,233.0
Direct investment:			
U.S. investment abroad	388.1	1,068.1	1,840.0
Foreign investment in the United States	127.1	824.1	1,505.2
Private portfolio investment in securities:			
U.S. investment abroad	62.5	1,751.2	1,846.9
Foreign investment in the United States	90.2	2,050.9	3,244.3

U.S. Corporate Profits[3]	**1960-69**	**1990-99**	**2000-2003**
Share from foreign sources	7.0%	17.9%	23.2%

Gross Domestic Product (GDP)[4]	**1965**	**1996**	**2003**
U.S. share of world total	39.9%	26.2%	30.4%

Population[5]	**1960**	**1996**	**2003**
U.S. share of world total	6.0%	4.7%	4.6%

Exports[6]	**1960**	**1996**	**2003**
U.S. share of world total	15.3%	11.7%	9.8%

Direct Investment Stock[7]	**1967**	**1996**	**2003**
U.S. share of world outward direct investment stock	50.4%	24.7%	21.9%

Table Notes:

[1] PwC calculations based on data from the U.S. Department of Commerce: U.S. International Transactions Accounts Table 2

[2] U.S. Department of Commerce: http://www.bea.gov/bea/di/home/iip.htm

[3] PwC calculations based on data from the U.S. Department of Commerce: NIPA Table 6.16C (line 6 divided by line 1).

[4] International Monetary Fund, "World Economic Outlook" April 2004.

[5] World Bank, World Development Indicators Online.

[6] International Monetary Fund, "International Financial Statistics Database."

[7] World Invetsment Report, United Nations Conference on Trade and Development, various years.

Exhibit 2. Tax Revenues as a Percent of GDP in OECD Country, 2001

[Revenues collected by national, state, and local governments]

Australia	30.1
Austria	45.4
Belgium	45.8
Canada	35.1
Czech Republic	38.4
Denmark	49.8
Finland	46.1
France	45.0
Germany	36.8
Greece	36.9
Hungary	39.0
Iceland	36.5
Ireland	29.9
Italy	42.0
Japan	27.3
Korea, Republic of	27.2
Luxembourg	40.7
Mexico	18.9
Netherlands	39.5
New Zealand	33.8
Norway	43.3
Poland	33.6
Portugal	33.5
Slovak Republic	32.3
Spain	35.2
Sweden	51.4
Switzerland	30.6
Turkey	36.5
United Kingdom	37.3
United States	28.9
Unweighted averages	
EU15	41.0
OECD	36.9

Source: OECD, *Revenue Statistics, 1965-2002,* 2003, Table 3.

Exhibit 3.—Tax Revenues by Source in OECD Countries, 2001

[Percent of total tax revenues collected by national, state and local governments]

Country	Income & Profit Taxes	Social Sec. & Payroll Taxes	Property Taxes	Taxes on Goods & Serv.	Other Taxes
Australia	55.6	6.3	9.0	29.1	-
Austria	31.5	38.8	1.3	27.1	1.1
Belgium	39.6	31.4	3.2	24.6	-
Canada	48.1	16.8	9.9	24.7	0.6
Czech Republic	23.5	44.6	1.3	30.5	-
Denmark	59.1	4.9	3.4	32.2	-
Finland	41.1	26.8	2.3	29.4	0.1
France	25.4	38.6	6.9	25.2	3.7
Germany	28.8	39.8	2.3	28.8	-
Greece	26.1	30.9	4.8	37.9	0.4
Hungary	25.6	33.1	1.8	38.7	0.7
Iceland	43.0	8.1	7.2	41.5	0.2
Ireland	41.8	14.5	5.8	37.3	-
Italy	34.2	29.0	4.8	25.6	6.1
Japan	32.8	37.7	10.3	19.0	0.3
Korea, Republic of	26.4	18.4	11.4	39.6	4.0
Luxembourg	36.0	27.4	9.7	26.6	0.1
Mexico	28.0	18.2	1.5	51.5	0.8
Netherlands	26.7	36.0	5.2	30.7	0.5
New Zealand	58.4	0.9	5.2	35.5	-
Norway	46.0	20.5	2.2	31.3	-
Poland	29.4	30.8	3.9	35.8	-
Portugal	28.9	27.0	3.1	40.0	0.5
Slovak Republic	20.6	44.5	1.7	33.2	-
Spain	28.2	35.9	6.4	29.3	0.3
Sweden	37.6	33.8	3.1	25.1	0.2
Switzerland	42.2	25.5	9.1	23.2	-
Turkey	27.8	19.7	2.3	38.7	11.5
United Kingdom	39.6	17.0	11.6	31.3	-
United States	48.8	24.6	10.6	16.1	-
Unweighted average:					
OECD Average	36.0	26.1	5.4	31.3	1.0

Note: Numbers may not add to 100% due to inclusion of customs duties in the total by the OECD.

Source: OECD (2003), Revenue Statistics, 1965-2002, Tables 7.

Exhibit 4.—Tax Revenues by Source in OECD Countries, 2001

[Tax revenues collected by national, state and local governments as a percent of GDP]

Country	1000 Income & profits	2000 Social security	3000 Payroll	4000 Property	5000 Goods & services	6000 Other
Australia	16.7	-	1.9	2.7	8.7	-
Austria	14.3	14.9	2.7	0.6	12.3	0.5
Belgium	18.1	14.4	-	1.5	11.3	-
Canada	16.9	5.1	0.7	3.5	8.7	0.2
Czech Republic	9.0	17.1	-	0.5	11.7	-
Denmark	29.4	2.2	0.3	1.7	16.0	-
Finland	19.0	12.4	-	1.1	13.6	-
France	11.4	16.3	1.0	3.1	11.3	1.6
Germany	10.6	14.6	-	0.8	10.6	-
Greece	9.6	11.4	-	1.8	14.0	0.1
Hungary	10.0	11.6	1.3	0.7	15.1	0.3
Iceland	15.7	3.0	-	2.6	15.2	0.1
Ireland	12.5	4.4	-	1.7	11.2	-
Italy	14.4	12.2		2.0	10.8	2.6
Japan	8.9	10.3	-	2.8	5.2	0.1
Korea	7.2	5.0	0.1	3.1	10.8	1.1
Luxembourg	14.7	11.2	-	3.9	10.8	-
Mexico	5.3	3.2	0.2	0.3	9.7	0.1
Netherlands	10.5	14.2	-	2.0	12.1	0.2
New Zealand	19.8	-	0.3	1.8	12.0	-
Norway	19.9	8.9	-	1.0	13.6	-
Poland	9.9	10.2	0.2	1.3	12.0	-
Portugal	9.7	9.1	-	1.0	13.4	0.2
Slovak Republic	6.7	14.4	-	0.5	10.7	-
Spain	9.9	12.6	-	2.2	10.3	0.1
Sweden	19.3	15.3	2.1	1.6	12.9	0.1
Switzerland	12.9	7.8	-	2.8	7.1	-
Turkey	10.1	7.2	-	0.9	14.1	4.2
United Kingdom	14.8	6.3	-	4.3	11.7	-
United States	14.1	7.1	-	3.1	4.6	-
Unweighted averages:						
OECD Total	13.4	9.4	0.4	1.9	11.4	0.4
EU 15	14.6	11.4	0.4	2.0	12.2	0.4

Source: OECD, *Revenue Statistics, 1965-2002,* 2003, p. 76.

Exhibit 5.—Highest Statutory Personal Income Tax Rates in OECD Countries, 2003

[Central government]

Australia	47.0
Austria	50.0
Belgium	50.0
Canada	29.0
Czech Republic	32.0
Denmark	59.0
Finland	35.5
France[1]	27.7
Germany	48.5
Greece	40.0
Hungary	40.0
Iceland[2]	26.1
Ireland	42.0
Italy	45.0
Japan	37.0
Korea, Republic of	36.0
Luxembourg	38.0
Mexico	34.0
Netherlands	52.0
New Zealand	39.0
Norway	19.5
Poland	40.0
Portugal	40.0
Slovak Republic	38.0
Spain	29.2
Sweden	25.0
Switzerland[3]	13.0/13.2
Turkey	40.0
United Kingdom	40.0
United States	35.0
Unweighted average	
OECD[4]	37.6

[1] Estimated rate for married taxpayers. Estimated top rate for single taxpayers is 35.7%

[2] 2001 Rate from OECD Tax Database.

[3] The top marginal rate is 13% for spouses living together and 13.2% for other taxpayers. For incomes over CHF 788,400 and CHF 664,300, respectively, the tax rate is 11.5%.

[4] Midpoint tax rate used for countries with multiple tax rates.

Source: PricewaterhouseCoopers, *Individual Taxes 2003-2004: Worldwide Summaries,* (2004).

Exhibit 6.—Highest Statutory Corporate Income Tax Rates in OECD Countries, 2003
[Central government]

Australia	30.0
Austria	34.0
Belgium	40.2
Canada	24.1
Cyprus[1]	10.0
Czech Republic	31.0
Denmark	30.0
Estonia[2]	0.0
Finland	29.0
France	36.3
Germany	26.5
Greece	35.0
Hungary	18.0
Iceland[3]	30.0
Ireland[4]	12.5/25.0
Italy	34.0
Japan	30.0
Korea, Republic of	27.0
Latvia	19.0
Lithuania	15.0
Luxembourg	22.9
Malta	35.0
Mexico	34.0
Netherlands	34.5
New Zealand	33.0
Norway	28.0
Poland	27.0
Portugal	33.0
Slovak Republic	25.0
Slovenia	25.0
Spain	35.0
Sweden	28.0
Switzerland	8.5
Turkey	30.0
United Kingdom	30.0
United States	**35.0**
Unweighted Averages: [5]	
EU 15	31.1
EU 25	26.6
OECD	29.3

[1] For tax years 2003 and 2004 only an additional 5% is imposed on taxable profits over C£1,000,000.

[2] For distributed profits (and certain non-business expenses) the rate is approximately 35%

[3] 2002 rate from OECD Tax Database.

[4] The standard rate (on trading income) is 12.5%. The rate on passive income is 25%.

[5] Midpoint tax rate used for countries with multiple tax rates.

Source: PricewaterhouseCoopers, *Corporate Taxes 2003-2004: Worldwide Summaries*, 2004.

Exhibit 7.—Taxation of Corporate Dividends in OECD Countries, 2003

No relief from double taxation of corporate dividends	Method of relieving double taxation of corporate dividends			
	Shareholder level			Corporate level
	Imputation system (partial or complete)	Tax credit method	Special personal tax rate	
Switzerland	Australia	Canada	Austria	Czech Republic[2]
	Finland[5]	France	Belgium[5]	Iceland[2]
	Mexico	Ireland	Czech Republic[2]	
	New Zealand	Rep. of Korea	Denmark	
	Norway	Spain	Germany[1]	
	Portugal		Greece[5]	
	United Kingdom		Hungary	
			Iceland[2]	
			Italy	
			Japan	
			Luxembourg[3]	
			Netherlands[4]	
			Poland	
			Sweden	
			Turkey	
			United States	

[1] Germany recently has adopted a 50 percent dividend exclusion.

[2] In addition to providing a lower tax rate for dividends in the personal income tax, the Czech Republic and Iceland allow corporations to partially deduct dividends. See Edwards (2003), "Nearly All Major Countries Provide Dividend Tax Relief" The Cato Institute.

[3] Luxembourg has a 50 percent dividend exclusion.

[4] The new Personal Income Tax Act of 2001, exempts from taxation dividends and most other investment income.

[5] Information as of 1996 based on S. Cnossen.

Sources:

1. PricewaterhouseCoopers, Individual Taxes 2002-2003: Worldwide Summaries (John Wiley & Sons, 2003), and
2. Sijbren Cnossen, "Reform and Harmonization of Company Tax Systems in the European Union," Research Research Memorandum 9604, Erasmus University, Rotterdam (1996).

Exhibit 8.--Combined U.S. Individual and Corporate Statutory Tax Rate: Corporate Income Distributed as a Dividend to Individual Shareholder in Top Bracket

2003 Law	
Corporate income	$100.00
Less corporate income tax at 35% (federal)	$35.00
Net income	$65.00
Dividend assuming 100% distribution	$65.00
Less individual income tax at 15.0% (federal)	$9.75
Net income after federal and individual income tax	$55.25
Combined corporate and individual income tax rate	***44.75%***
2011 Law	
Corporate income	$100.00
Less corporate income tax at 35% (federal)	$35.00
Net income	$65.00
Dividend assuming 100% distribution	$65.00
Less individual income tax at 39.6% (federal)	$25.74
Net income after federal and individual income tax	$39.26
Combined corporate and individual income tax rate	***60.74%***

Source: PricewaterhouseCoopers calculations.

Exhibit 9.—U.S. Government Statement of Social Insurance: Present Value of Long-Range Actuarial Projections

[Billions of dollars]

Item	Expenditures	Revenues	Revenues less Expenditures
Social security	$31,075	$26,148	-$4,927
Medicare A	$14,577	$8,411	-$6,166
Medicare B	$12,773	$3,120	-$9,653
Total	$58,425	$37,679	-$20,746

Source: General Accounting Office, *Financial Statement of the U.S. Government* , 2003

Exhibit 10.—Effective Average Tax Rate for Investment into EU

Investment from MNC based in:	Financing of foreign subsidiary			
	Retained earnings	New equity	Debt	Average
EU	30.10%	30.40%	30.20%	30.20%
US	33.20%	35.70%	34.70%	34.50%

Source: Commission of the European Communities, "Towards an Internal Market without Obstacles," Com(2001)582, Brussels, October 23, 2001.

Exhibit 11.—Taxation of Foreign Subsidiary Dividends in OECD Countries, 2003

Dividend exemption ("territorial")[3]	Worldwide taxation
1. Australia	1. Czech Republic
2. Austria	2. Greece
3. Belgium	3. Iceland[2]
4. Canada	4. Japan
5. Denmark	5. Rep. of Korea
6. Finland	6. Mexico
7. France	7. New Zealand
8. Germany	8. Norway
9. Hungary	9. Poland
10. Ireland[1]	10. Portugal
11. Italy	11. Turkey
12. Luxembourg	12. United Kingdom
13. Netherlands	13. United States
14. Spain	
15. Sweden	
16. Switzerland	

[1] Although Ireland nominally has a worldwide tax system, under the Finance Act of 1988, foreign subsidiary dividends generally are exempt if re-invested in employment-generating activities within Ireland.

[2] Information as of 1990 based on OECD.

[3] Dividend exemption by statute, treaty, or listed countries.

Source: PricewaterhouseCoopers, *Corporate Taxes 2003-2004: Worldwide Summaries,* (2004).